AUDIT DIVISION STATISTICAL STUDY

The following information is based on 100% of the audits completed, taxpayers assisted and special projects conducted during Fiscal Year 2002, and addresses the requirements set forth by IC 6-8.1-14-4(2).

See Page 39 for an Index of exhibits and charts included.

TAXPAYERS SERVED IN DISTRICT OFFICES

Taxpayer assistance is available in all district offices. Each office has a taxpayer assistance supervisor and assistant taxpayer assistance supervisor who perform taxpayer service functions as well as other office support responsibilities.

The "Taxpayer Assistance Report" (Exhibit A) provides the number of taxpayers assisted (in person and by telephone) and the amount of money collected and assessed in each office by the taxpayer assistance program. Exhibit A reveals that during Fiscal Year 2002 district offices assisted 164,295 taxpayers in person and 206,195 taxpayers through telephone contact. Total number of taxpayers served by the district offices was 370,490. The district office in Columbus served 27,070 taxpayers in person, the highest number of any district office. The Lafayette District Office served 23,421 taxpayers in person, the second highest total.

The Merrillville District Office served 28,995 taxpayers by telephone while the Lafayette District Office served 22,975 taxpayers by telephone. This was the highest number of telephone contacts among the district offices, representing 14% and 11% respectively. The Columbus District Office served a total of 47,715 taxpayers by telephone and walk-in assistance while Lafayette served 46,396 taxpayers by telephone and walk-in assistance.

"Taxpayer Assistance/Special Project Statistics" (Exhibit B) provides the number of hours devoted by field auditors in the district offices to assist taxpayers and conduct special projects. The exhibit reveals that 11,231 auditor hours were channeled in this direction.

SPECIAL PROJECTS

The Audit Division pursued three special projects during the 2002 Fiscal Year.

Project Comply 2002 commenced at the conclusion of Project Comply 2001 and was conducted statewide. These audits identified candidates that were usually small and would normally not meet the criteria for a regular audit examination. The results of Project Comply 2002 are:

Audits Completed	836
Assessments	$1,728,371
Refunds	$ 109,389

The Prepaid Telephone Card project was also conducted statewide. Effective July 1, 1998 the sale of prepaid telephone cards became a retail transaction subject to sales tax. To ascertain compliance, auditors visited 2,567 locations. The results of this project are:

Number of Non-Compliant Locations	527
Sales Tax Assessed/Collected	$267,907

A Truck Stop Survey was also conducted during this fiscal year. The purpose of this project was to survey various distributors and review the records of selected independent truck stops to ensure that special fuel tax was being paid on the sale of diesel fuel. No compliance issues were discovered.

GROSS INCOME TAX VIOLATIONS

The most frequently violated gross income tax rule is 45 IAC 1.1-2-5. This rule defines taxability of gross receipts from services. Violations (39) of this rule accounted for 11.82% of all violations of the gross income tax rules in the statistics. This was also the most frequently violated rule in the previous two studies, accounting for 16.03% in 2001 and 14.50% in 2000.

The second most frequently violated gross income tax rule is 45 IAC 1.1-3-3. This rule defines the interstate commerce exemption as applied to gross receipts tax. Rule 3-3 was inappropriately applied according to regulations affording taxpayers more exclusions from gross receipts. 45 IAC 1.1-3-3 produced 35 (10.61%) gross income tax rule violations. This rule was the second most frequently violated gross income tax rule in the 2001 study (8.75%) and the 2000 study (10.32%).

Ranking third with 30 (9.09%) infractions of the gross income tax rule violations is Rule 45 IAC 1.1-2-2. This rule defines taxable low rate gross income of retail and wholesale sales, display advertising, dry cleaning and laundry service, rental of water softening equipment, rental of rooms, lodging, booths and similar accommodations and commercial printing. Rule 45 IAC 1.1-2-4 defines taxable high rate income of utilities, display advertising, sale of real estate, rentals and extension of credit and was the third most violated rule in the 2001 report with 7.87%. The third most frequently violated rule for 2000 was 45 IAC 1.1-1-10 at 8.85%. This rule defines receipts to mean the entire gross income or gross receipts received by a taxpayer, actually or constructively, without any deduction of any kind or nature. In 1999, the third most violated rule was 45 IAC 1-1-213 at 5.94% which requires withholding from all payments to a nonresident contractor.

SALES/USE TAX VIOLATIONS

The most frequently violated sales and use tax rule is 45 IAC 2.2-3-20. Rule 3-20 states that if the seller of tangible personal property for storage, use or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit tax directly to the department. This rule produced 605 violations (12.72%) of the sales and use tax infractions. In 2001, 45 IAC 2.2-6-8, which discuses the determination of a retail merchant's liability for a report period, was violated 14.92% or 614 times.

The second most frequently violated sales and use tax rule is 45 IAC 2.2-5-8. Rule 5-8 clarifies sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools, and equipment used in direct production and other activities. This rule accounted for 535 infractions or 11.25% of sales and use tax statute violations. 45 IAC 2.2-3-20 (explained above) was the second most violated rule in the 2001, 2000 and 1999 studies accounting for 500, 664 and 615 violations respectively.

The third most violated rule for the 2002 fiscal year is 45 IAC 2.2-3-4. Rule 3-4 imposes use tax on "tangible personal property, purchased in Indiana, or elsewhere in a retail transaction, and stored, used or otherwise consumed in Indiana . . . unless the Indiana state gross retail tax (sales tax) has been collected at the point of purchase." Failure of taxpayers to comply with this rule accounts for 518 or 10.89% of the sales and use tax infractions. This rule ranked third in 2001 with 481 violations but ranked first in violations in 2000 and 1999. Fiscal year 2000 showed 694 violations and 1999 showed 658 violations.

■ CORPORATE ADJUSTED GROSS INCOME TAX VIOLATIONS

Corporate taxpayers violated adjusted gross income Rule 45 IAC 3.1-1-8 more than any other rule. This rule states that taxable income as defined in the Internal Revenue Code is modified in several ways to arrive at Indiana adjusted gross income. Violations (94) of this rule accounted for 12.21% of the total violations. Rule 1-8 was also the most violated rule in 2001 with 119 or 13.52% of total infractions. The 2000 and 1999 report revealed Rule 1-97 ranked first for adjusted gross income infractions with a 22.00% and 21.78% violation rate.

Rule 45 IAC 3.1-1-9 was the second most frequently violated rule under this study. This rule deals with the adoption of modifications as defined in the Internal Revenue Code. More specifically, it allows a net operation loss as a deduction in computing Indiana Adjusted Gross Income (IRS Code Section 172). These violations (79) account for 10.26% of the total violations for 2002. 45 IAC 3.1-1-97 ranked second in the 2001 study with 115 violations accounting for 13.07% of the total violations.

The third most frequently violated rule is 45 IAC 3.1-1-97. Rule 1-97 addresses the returns and reports that must be filed by adjusted gross tax withholding agents. Violations (72) of this rule accounted for 9.35% of the violations of adjusted gross income tax rules. 45 IAC 3.1-1-9 (noted above) was the third most violated rule in the 2001 study accounting for 90 or 10.22% of the violations of adjusted gross income tax rules. The 2000 and 1999 violations of 45 IAC 3.1-1-9 also ranked third with 8.62% and 8.19% respectively.

■ AMOUNTS OF TAX ASSESSED

Exhibits C, D and E display the amount of assessments (refunds) and violations of the gross income tax, sales tax and adjusted gross income tax administrative rules, respectively. "Total assessments" for any tax type represent gross assessments less amounts refunded.

The amount assessed or refunded for each of the most frequent violations and the percentage of the amount to total net assessments are presented below:

Gross Income Tax—Exhibit C:

	Amount Assessed	Percentage of All Assessments
45 IAC 1.1-2-5	$3,356,813	12.19%
45 IAC 1.1-3-3	$8,148,159	29.58%
45 IAC 1.1-2-2	$4,534,187	16.46%

Sales/Use Tax—Exhibit D:

	Amount Assessed	Percentage of All Assessments
45 IAC 2.2-3-20	$2,027,614	11.44%
45 IAC 2.2-5-8	$6,871,170	38.78%
45 IAC 2.2-3-4	$3,105,696	17.53%

Corporate Adjusted Gross Income Tax—Exhibit E:

	Amount Assessed	Percentage of All Assessments
45 IAC 3.1-1-8	$ 6,262,911	31.10%
45 IAC 3.1-1-9	($ 4,454,763)	(22.12)%
45 IAC 3.1-1-97	$ 417,075	2.07%

■ INDUSTRY/BUSINESS/MOST FREQUENTLY IN VIOLATION

Gross Income Tax

For the tenth consecutive time, taxpayers engaged in manufacturing most frequently violated the gross income tax rules. This group committed 82 violations or 24.85% of the total violations. The gross income tax rule most frequently violated by this group of taxpayers was 45 IAC 1.1-3-3. This rule defines the exemption of gross receipts derived from business conducted in interstate commerce.

The second largest number of gross income tax violations was committed by taxpayers providing information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services. This group committed 66 infractions or 20.00% of the total violations for 2002. The most frequently violated rule of this group was 45 IAC 1.1-3-3. This group had 20.99% of total violations in the 2001 study. The service industry ranked second in the 1999 study. Wholesalers and retailers were the second most frequent violators of these rules in the 1998 and 2000 studies.

Sales and Use Tax

For the 2002 reporting period, repair, personal services and other services are the industries with the most infractions. They accounted for 1,055 violations or 22.18% of the total sales and use tax violations. The most frequently violated rule by these taxpayers was 45 IAC 2.2-3-20, which deals with remitting use tax on transactions where the seller doesn't collect the sales tax.

Manufacturing businesses had the second most frequency of violations of the sales and use tax rules. There were 788 violations committed by this group representing 16.57% of the total violations. The rule most frequently violated by this group was 45 IAC 2.2-5-8, which clarifies taxable and nontaxable sales of machinery, tools and equipment used in direct production.

Adjusted Gross Income Tax

Repair, personal service and other service providers with 218 infractions, were the most frequent violators of adjusted gross income tax rules. This figure represents 28.31% of the total adjusted gross income tax violations. 45 IAC 3.1-1-1, which defines adjusted gross income for individuals in relationship to Section 62 of the Internal Revenue Code, accounted for the most infractions in this class.

The information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services industries were the second most frequent violators of the adjusted gross income tax rules. They committed 165 infractions or 21.43% of the adjusted gross income tax violations. 45 IAC 3.1-1-97 was the most violated rule by these industries. Rule 1-97 specifies the returns and reports that must be filed by withholding agents for adjusted gross income tax purposes.

■ SPECIAL TAX VIOLATIONS

Exhibit G provides the number of special tax rule violations and the amount of special tax assessments and refunds.

Article VIII (citation R800 on exhibit) of the International Fuel Tax Agreement (IFTA) was the most frequently violated special tax item in the study. It specifies the taxable event is the consumption of motor fuels in the propulsion of qualified motor vehicles, except fuel consumed that is exempt from taxation by a jurisdiction. All motor fuel acquired that is normally subject to consumption tax is taxable unless proof to the contrary is provided by the licensee. Article VIII was violated 197 times and yielded $483,585 in net assessments for the State of Indiana. This represents 26.80% of total violations.

The exhibit also reveals that Article X (citation R1000 on exhibit) of the International Fuel Tax Agreement (IFTA) was the second most frequently violated section of the special tax statutes. This Article discusses how taxpayers can obtain credit for tax previously paid on purchases of fuel at the pump. It also lists the records needed to substantiate the refund request. This article was violated 183 times accounting for 24.90% of the total violations. These violations resulted in a net refund of ($134,402).

The taxpayer group most frequently in violation of the special tax statutes and IFTA Articles was the wholesale, retail and transportation industries. This group committed 351 violations accounting for 47.76% of the total infractions. Article VIII of the International Fuel Tax Agreement was most frequently violated by the wholesale, retail and transportation industries.

■ MISCELLANEOUS CODE VIOLATIONS

Exhibit F provides the number of violations and assessment amounts of the following:

Financial Institutions Tax
Tax Administration
Food and Beverage Tax
Innkeeper's Tax

A review of this exhibit reveals that IC 6-8.1-4-2 was violated 24 (14.46%) times in the 2002 study. This code section addresses access to accounting records of a business and the use of sampling techniques for auditing purposes. These violations yielded ($48,053) in net refunds. 45 IAC 15-9-2 was the most violated rule in the 2001 study. Rule 9-2 defines the statute of limitations as it applies to refunds.

The 20 violations of 45 IAC 15-9-2 yielded a total of $292,236 in assessments. Rule 9-2 is defined above. IC 6-8.1-4-2 also defined above, was the second most violated citation in the 2001.

■ NUMBER OF YEARS IN THE AUDIT PERIOD

The audit period consistently averages three years.

■ USE OF PROFESSIONAL TAX PREPARATION ASSISTANCE

The services of professional prepares were used in the preparation of 75.5% of the corporate income tax returns and 11% of the sales tax returns. These findings remain consistent with the previous years' reports.

■ FILING OF APPROPRIATE TAX RETURNS

Rule 45 IAC 3.1-1-92 (Exhibit E) requires qualifying corporations to make estimated tax payments. Taxpayers in violation of this rule either failed to file estimated income tax returns or failed to remit the appropriate amount of tax. For the fiscal year ending in 2002, the study indicates 12 violations of this rule, resulting in assessments in the amount of $825,255 and refunds totaling ($662,533).

Indiana Code 6-8.1-10-2.1 (Exhibit F) revealed no violations during the 2002 study period. This section specifies the penalty to be imposed if a taxpayer fails to file an appropriate return or pay the full amount of tax due. Violations of this section in the 2001, 2000 and 1999 studies were zero while the 1998 report showed one violation.